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BlackRock®

Global Real Assets Outlook 2020

Cycling slowly, relatively attractive, changing with the future.

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Alan Synnott
Global Head of Real Assets Research & Strategy

alan.synnott@blackrock.com

Simon Durkin
Head of European Real Assets Research

simon.durkin@blackrock.com

Steven Cornet
Head of US Real Assets Research

steven.cornet@blackrock.com

Bruce Wan
Head of Asia Real Assets Research

bruce.wan@blackrock.com

Cynthia Parpa
European Real Assets Research

Alex Symes
US Real Assets Research

Eric Tawney
US Real Assets Research

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Cover images:
Distributed solar portfolio – Massachusetts, US
Office building – Sydney, Australia.

Summary

We enter 2020 with a base case of moderate economic growth but a watchful eye on geopolitical risk. Absent any major shocks, we believe three key themes will drive the industry narrative this year: a long and slow cycle, strong relative value and movement towards a future shaped by powerful structural trends including demographics, sustainability, technology and policy.

This juxtaposition of continuity and significant change is particularly relevant for Real Assets investors. With interest rates near their lower bound, Real Assets continue to offer good relative value and attract significant capital flows. Fundamentals remain sound, though return expectations have moderated. It's easy to think of reasons broad market sentiment could change — a flare-up in the US-China trade conflict or a turn for the worse in the Middle East, for example — but for now, a slightly nervous normalcy persists.

Yet beneath this relatively calm exterior, deeper shifts are shaping the future in ways that some long-duration real estate and infrastructure assets are already prepared for. In his 2020 letter to CEOs, BlackRock's Larry Fink writes about the fundamental reshaping of finance resulting from climate change and the intensifying push for sustainability. At the same time the transformative impact of digital technology combines with politics and policy to drive dispersion in ways both obvious and less apparent. In real estate, the connection

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between online shopping, the rise of logistics properties and the woes in retail real estate are not hard to see. A bit subtler is the connection between densification in urban tech hubs and the push for residential rent control in some US states.

Identifying these cross-currents and sharing our thoughts on how to navigate them is our goal in this Outlook. Among our key observations:

- Despite record amounts of undeployed capital amid highly competitive markets, we expect capital flows to remain robust as investors seek returns in a low-rate world.
- In infrastructure, we expect renewable energy again to be the sector with the most investment activity, following a year when it accounted for more than 50% of investment activity. Given the scale and urgency of the power and energy transition underway around the world — and continuing technical and cost advances — we think this trend has a long way to run.
- In real estate, fundamentals remain positive, and returns will continue to be driven by income as the cycle slows. Market relativities will come to the fore as investors search for market selection value in a rapidly changing market environment increasingly driven by focus on sustainable investing and technological change.

Real Assets Key Themes 2020

1 Cycling slowly

2 Relatively attractive

3 Changing with the future

Setting the scene: market overview

Real Asset markets are both global and highly local. Here we offer a high-level view of the macroeconomic forces driving growth around the world, with some detail on geographic and sector variations.

Modest global growth, monetary easing and elevated geopolitical risk

The BlackRock Investment Institute 2020 Global Outlook: Testing limits sees a modest uptick in growth potentially disrupted by trends such as trade tensions and populism. The confrontation between the US and Iran adds another dimension of geopolitical risk, with potential ramifications for energy markets in particular.

Global monetary easing — including a dramatic turnabout by the US Fed — was probably the biggest single driver of Real Asset activity in 2019. Amid threats to growth that included a manufacturing slowdown, fallout from the US-China trade conflict and uncertainty over Brexit, Central Banks were quick to respond.

In 2020, we expect a follow-through economic response to the liquidity provided by Central Banks and hence expect modest upticks in growth globally. Healthy household spending (supported by low unemployment) in the advanced economies will provide some protection against the uncertainties impacting other sectors of the global economy. Elevated geopolitical risk as discussed in BlackRock's Geopolitical Risk Index[1] continues to be the main driver of economic volatility. We expect a respite on two fronts during 2020 thanks to the Phase One US-China trade deal and greater certainty over Brexit following the decisive Conservative win in the UK, but the potential for volatility remains.

Against this economic backdrop, Central Bank accommodation and yet lower sovereign yields have further pushed investors out of bonds and into equities and alternatives in search of higher returns. We summarize changing market conditions in the table below.

Continued strong capital flows

In 2019, capital raising for Real Assets remained strong at near record levels. Closed-end real estate and infrastructure funds saw inflows of US$185bn,[2] not far from a strong 2018. Infrastructure fundraising reached US$65bn, as of Dec 2019, which remained robust by historical standards. Closed-end real estate funds raised US$120bn in another strong year for the sector.

BlackRock's 2020 Global Rebalancing Survey indicates that approximately 55% of investors surveyed intend to increase their Real Assets allocations in 2020, moving out of equities and cash and into alternatives. This is significantly higher than all other asset classes and reflects investor demand for long duration assets and higher returns. The high proportion of no change across assets classes reflects the deployment challenges at a mature stage in the cycle.

Capital deployment is competitive

Deciding to invest in Real Assets continues to be easier than putting the capital to work. Global transaction volumes moderated in 2019 compared with the 5-year average (see Chart 2). According to Preqin,[3] dry powder hit new record highs, slightly up from last year at US$540bn. Real estate decreased slightly by 6% in 2019, whereas infrastructure dry powder increased almost 15%, reflecting an increasingly competitive investment landscape. This remains a fundamental trend as we move into 2020.

Chart 1: The evolution of market conditions

	Fundamentals	2017	2018	2019
Macro	Interest rates	▲	▼	▲
	Geopolitics	▲	▼	▼
	Capital markets	▲	▼	▲
Real Assets	Demand	▲	▲	▲
	Capital formation	▲	▲	▲
	Transactions activity	▲	▼	▼

▲ Constructive ▼ Challenging

1 BlackRock Investment Institute: Blackrock geopolitical risk dashboard, December 2019. **2** Preqin 9th December 2019, global fund raising and dry powder, closed-ended funds. **3** Preqin 9th December 2019, global fund raising and dry powder, closed-ended funds.

In infrastructure, renewables rule

In 2019, infrastructure deal flows moderated from an extremely strong 2018.[4] Despite slowing activity globally, renewable energy remained the largest sector in terms of investment activity, according to IJGlobal, accounting for more than 50% of transactions and is in line with the energy transition mega trend. Furthermore, this high level of activity is also consistent with the International Energy Agency's base case of the globe transitioning from a power mix that is two-thirds fossil fuel-based today, to one that is two thirds renewables-based by 2050. The remaining fossil fuel share will likely change to one that is focused on cleaner-burning natural gas. Investors want to participate, both for their own sustainability agendas and the stability and predictability of cash flows, combined with more certainty of a future exit. Transport and digital infrastructure also performed strongly reflecting the growing demand for these sectors.

Real estate transactions impeded by caution

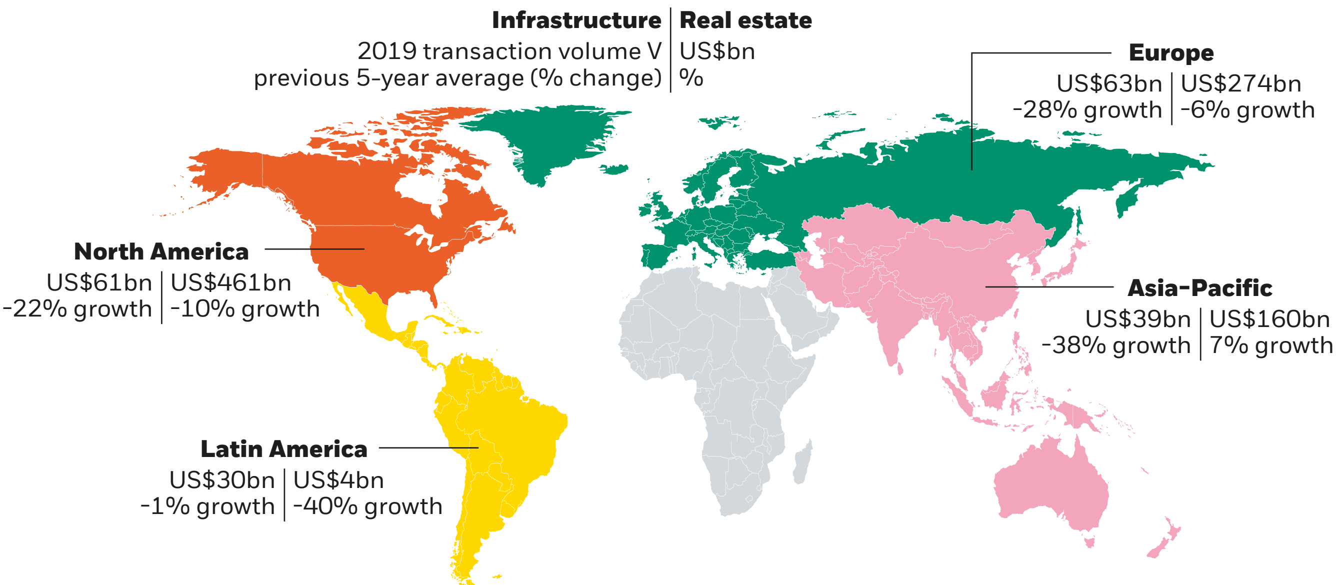
Global real estate volumes remained elevated but moderated over the course of 2019 compared with the record levels of 2018. Real estate investment activity generally tracks economic sentiment and as such it is unsurprising that global real estate volumes have moderated somewhat over the course of the year. However, considering the growth in global capital formation, the slowdown in transaction activity is also driven by lack of available suitable assets and investor caution.

Regionally, Europe led the decline in real estate transactions activity with an estimated decline of 6% against its 5-year average, driven largely by the UK, which was surpassed by Germany as the most liquid market in Europe in 2019. Despite the slowdown and Brexit uncertainty, London remains the first destination for global capital into Europe.

Asia Pacific markets have continued to attract strong transaction activity despite the elevated global geopolitical uncertainties and the ebb and flow of trade tensions. Tokyo is likely to close out 2019 as the most liquid market, replacing Hong Kong, which has suffered from falling volumes against a backdrop of social unrest.

In the US, volumes are estimated to be down 5% for the year compared to 2018, and approximately 10% down on the 5-year average. New York remains the most active transaction market globally, despite an almost 10% year-over-year decline in transactions. Tech-focused cities such as Austin, San Francisco and Seattle experienced elevated activity in 2019. In line with the other two regions, the challenges besetting the retail sector continue to reduce the available investment set for investors, as nearly all investors are bearish on the outlook for the sector. Furthermore, sellers have not adjusted price expectations to a level that prompts value investors.

Chart 2: Transaction markets remain reasonably active

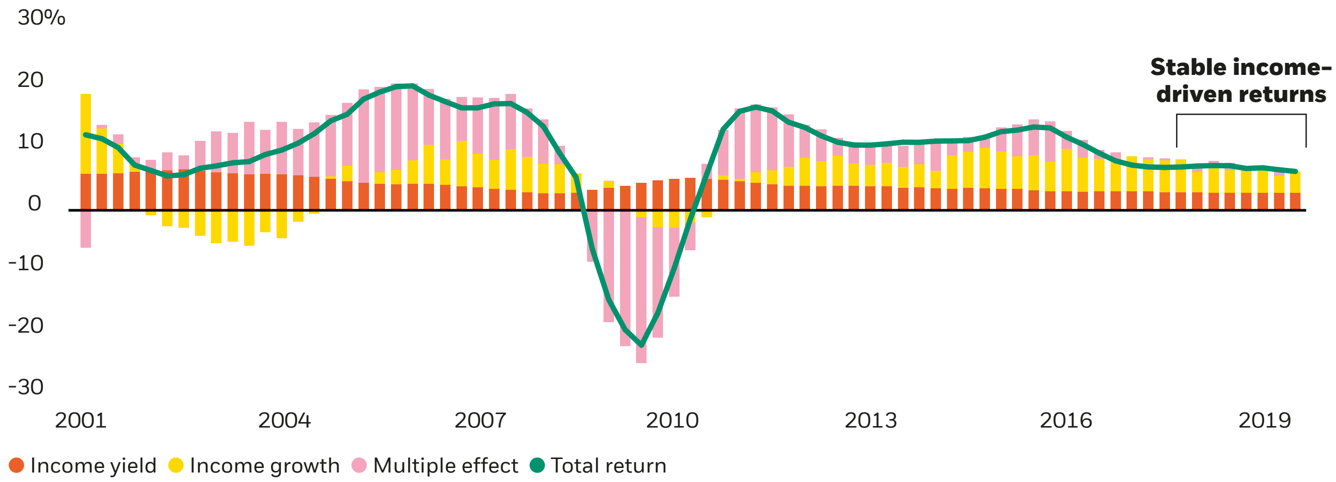


Source: Real Capital Analytics, IJGlobal, BlackRock (December 2019). RCA global real estate transaction volume data for income-producing properties excludes land development. IJGlobal global infrastructure transaction volume data reflects project finance equity and debt, and excludes sectors outside BlackRock's definition of infrastructure, such as metals and mining, oil and gas exploration and petrochemicals. All data is presented in USD, and percentage changes may be affected by non-USD currency fluctuation versus the USD. * Real estate data incorporate estimates from RCA produced in December 2019 for full year 2019, and infrastructure data refers to 12-month transaction volume as of November 2019.

4 IJGlobal.

Chart 3: Continued stable income-driven performance from real estate

Components of total return of US real estate (NCREIF Property Index, NPI)



Source: NCREIF, BlackRock (December 2019). **The figures shown relate to past performance.** Past performance is not a reliable indicator of current or future results. The components of total return are income yield, income growth (net operating income growth) and multiple effect (capitalization rate-shift effect).

Demand fundamentals are sound

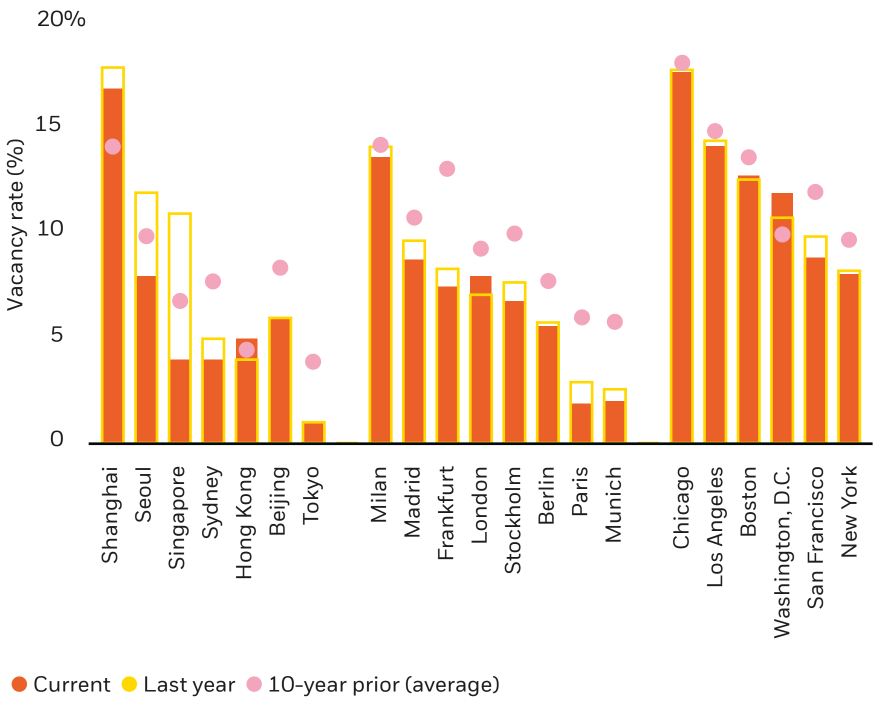
The performance of Real Assets was healthy in 2019, in line with the low return volatility of recent years. Income remained the driver of global Real Asset market returns, which is expected to continue in 2020, supported by constructive fundamentals. While appreciation returns have moderated, as shown in Chart 3, ultra-low interest rates globally are supportive of current valuations. However, we foresee a growing risk in pricing, particularly in core markets and stabilized projects where investor demand remains elevated, weight of capital high and opportunities keenly priced.

Within real estate, occupancy is stable at levels well above long-term averages in most sectors and most markets, as highlighted by Chart 4. This is supportive of a continuation of a low volatility, income-driven environment. New deliveries have remained at manageable levels to absorption, and with such a supply and demand dynamic, rent growth is also healthy. Relative attractiveness across regions means that markets are exhibiting unsynchronized and differentiated cycles, geared more directly to specific regional economic and real estate factors. We also need to look beyond geographic and sector diversification. Today, more than ever, markets are exhibiting relationships and differentiation driven by factors such as emerging employment sectors, ecosystems of academic institutions and regional culture and government policy on areas such as mass transit, taxation and rent regulation.

Risks, more than ever before, are emerging from disruptors within the sector. This is evident in the late 2019 WeWork saga. Coworking, which was a significant driver of absorption in major global office markets in 2019, is likely to slow as investor appetite for the space, particularly within venture capital, slows. E-commerce globally continues to be a significant driver of retail and industrial returns,

Chart 4: Global occupier markets are holding up

Major office markets vacancy rate (%)



Source: BlackRock, PMA, REIS, JLL as of September 2019.

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and this is likely to accelerate further. In multifamily, the emergence of Airbnb enabled short-term stay operators to move into the space and is introducing credit and hospitality risk into the sector.

combined with more aggressive government renewable energy standards and a rise in corporate power purchase agreements (PPAs) is resulting in accelerating demand for renewable power generation.

The structure of energy delivery is also shifting with the growing emergence of distributed renewable generation, creating both challenges and opportunities for existing energy infrastructure.

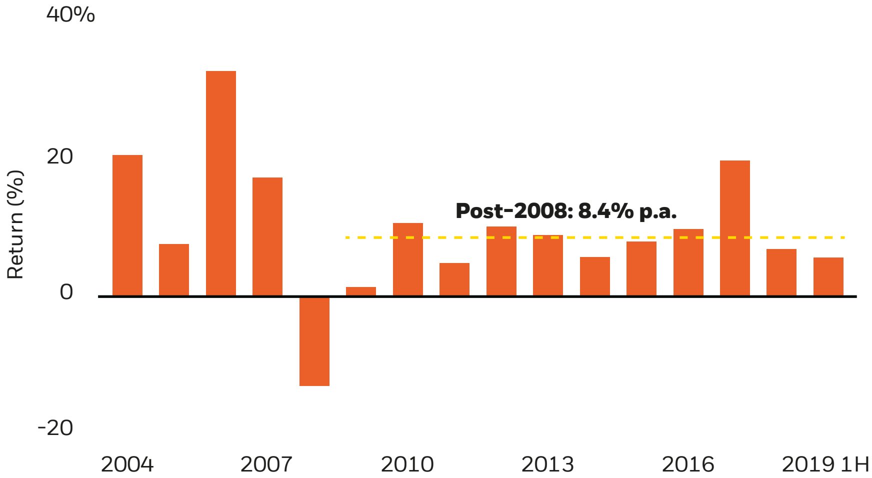
Stable infrastructure performance but variability among sectors

The return performance of private infrastructure (see Chart 5) has also remained positive in the year to 2H 2019 delivering a robust 5.7% annualized return. And like real estate, performance has been driven largely by income rather than the multiple expansion experienced over recent years.

Within infrastructure, the shift to natural gas and renewable energy consumption is continuing in earnest. Abundant production in the US, for instance, is fuelling demand for pipelines to transfer natural gas from production sources and power plants to process into consumable power, presenting opportunities for investors. Meanwhile, the significant improvements in cost competitiveness of renewables,

Chart 5: Private infrastructure funds continue to deliver sustained returns

Cambridge Associates Infrastructure Index: Annual Performance (USD)



Source: Cambridge Associates LLC (December 2019). Performance data is latest available, shown as of June 2019. The index is a horizon calculation based on data complied from infrastructure funds, including fully-liquidated partnerships, formed between 1993 and 2017. Performance is shown in US dollar terms, net to limited partners. The figures shown relate to past performance. **Past performance is not a reliable indicator of current or future results.**

Listed Real Assets – strong earnings make for a good year

Listed Real Assets are well positioned for 2020. Market fundamentals are generally in balance across the sector, which is supportive of earnings growth. Companies on aggregate should be net buyers of assets in the coming year. Strong stock performance and low interest rates may support either public-to-public M&A or transactions from the private market. Adding in the sector's relatively high dividend payout ratios should result in constructive returns in the coming year.

At the same time, there will likely be noticeable dispersion between and within subsectors during the coming year. Retail real estate provides an excellent example, with operators of class A retail properties better-positioned for growth than operators with lower-quality portfolios. In the power space, more-regulated utilities with stable income growth could outperform less-regulated peers. Regulated utilities are benefiting from a low cost of capital, even as some regulated rates are under pressure across various local jurisdictions. This should result in an attractive return on equity and a maintenance of relatively attractive earnings and dividends. As we move later in the cycle, management strength will likely be a clear differentiator. This will be especially true as operators are navigating higher levels of disruption than in years past.

The listed space is also uniquely positioned to provide investors instant and liquid access to the subsectors that are rapidly evolving for the future. The growth in demand for digital infrastructure, e.g. cell towers and data centers, will be robust during the next few years. And demographics support growth in senior housing and medical office. Listed companies provide an avenue for Real Asset investors to access these exposures and operating expertise to achieve alpha and diversification goals, while maintaining liquidity.

Real Assets Key Themes 2020

1 Cycling slowly

The recent slowdown in the global economy had only a moderate impact on Real Assets market activity. In real estate, occupier demand remains strong where vacancy rates have fallen over the past 12 months and are significantly below their long-term average in most global markets.

Moderate global economic growth for the foreseeable future has set in and appears to be the new normal. At the same time, usual late-cycle limits, most notably an overheating in factors such as wage and price inflation that would prompt central banks to tighten even as recession risks rise, are not visible. On the contrary, interest rates fell during the year. As a result, we believe we are in a slow-moving cycle or to say it differently: even lower for even longer.

In this environment of moderate growth and low rates, Real Assets fundamentals remain sound (as discussed in the previous section). New construction remains in check in a vast majority of global real estate and infrastructure markets, with a combination of disciplined lending markets and structural barriers such as higher construction costs and policy uncertainties. As a result of this relative demand-supply balance, and in line with the last few years, income growth has driven healthy and stable Real Assets returns.

While from a high level, the market may appear similar to 2019, there are divergences across both sectors and markets (more on that in the next theme). Even though we have experienced an unusually long and stable cycle, cycles are not dead; rather, they are stretched and bumpier. In such a market it is important to remain cognisant of any emerging imbalances. Patience, risk control and flexibility remain critical.

We are also seeing cracks emerging in the publicly-listed and debt markets. Within listed strategies, there is an increasing polarisation. Strong management teams with higher-quality assets and better-capitalized businesses are outperforming while weaker management teams and businesses are struggling. Within the debt space, yields have tightened for deals, there are some signs of stretching on underwriting assumptions. However, in Europe, only the largest sponsors are able to secure covenant-light structures.

2 Relatively attractive

Risk-adjusted returns from Real Assets remain attractive relative to other asset classes amidst the stable 'lower for longer' interest rate environment and a backdrop of negative policy rates in several of the world's major economies.

Forward return expectations across asset classes are moderating, as detailed in our BlackRock Capital Market Assumptions. This has compelled investors to reconsider their asset class allocation in favour of income producing Real Assets.

Investors are increasingly shifting allocations to the Real Assets sector and entry yields offer favourable relative spreads to risk-free rates, see Chart 6.

Although we had expected yield compression (or multiple expansion) to come to an end last year, the movement lower in interest rates and increased Central Bank accommodation across the globe has us more convinced that moderate valuation gains are still possible in some markets.

However, while we remain positive on valuations given the market backdrop, we must recognize that asymmetric risk is rising. With prices tight, the likelihood of a shock to the downside outweighs the likelihood of significant moves higher. The tighter market relationship to binary outcomes such as future Central Bank rate decisions, geopolitical trade issues and policy developments mean investors need to be more aware of their risk exposure.

Even in the bounds of a single Real Assets sector we see dispersion. The global renewable power market for example offers investors a variety of potential financial outcomes, with divergence in contracted revenues, size of opportunity and supply of capital all influencing returns, as illustrated in Chart 7. Demand is very tight for long contracted revenues, particularly in OECD countries. This is leading some

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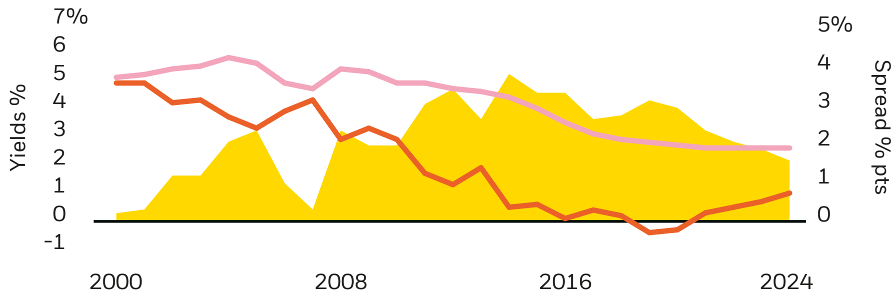
participants to reach into more opportunistic assets as well as into emerging asset classes. We see the same characteristics with natural gas and oil infrastructure investments, showing the strong appetite for core stabilized assets.

In real estate we see dispersion across sectors and cities. From a sector perspective, industrial properties are outperforming across regions while returns on retail properties remain muted. Meanwhile, across cities we are seeing outperformance in global secondary cities benefiting from tech and professional business service employment gains. In the box below, we discuss how this creates relative value opportunities.

Chart 6: Relatively attractive in a "lower for longer" environment

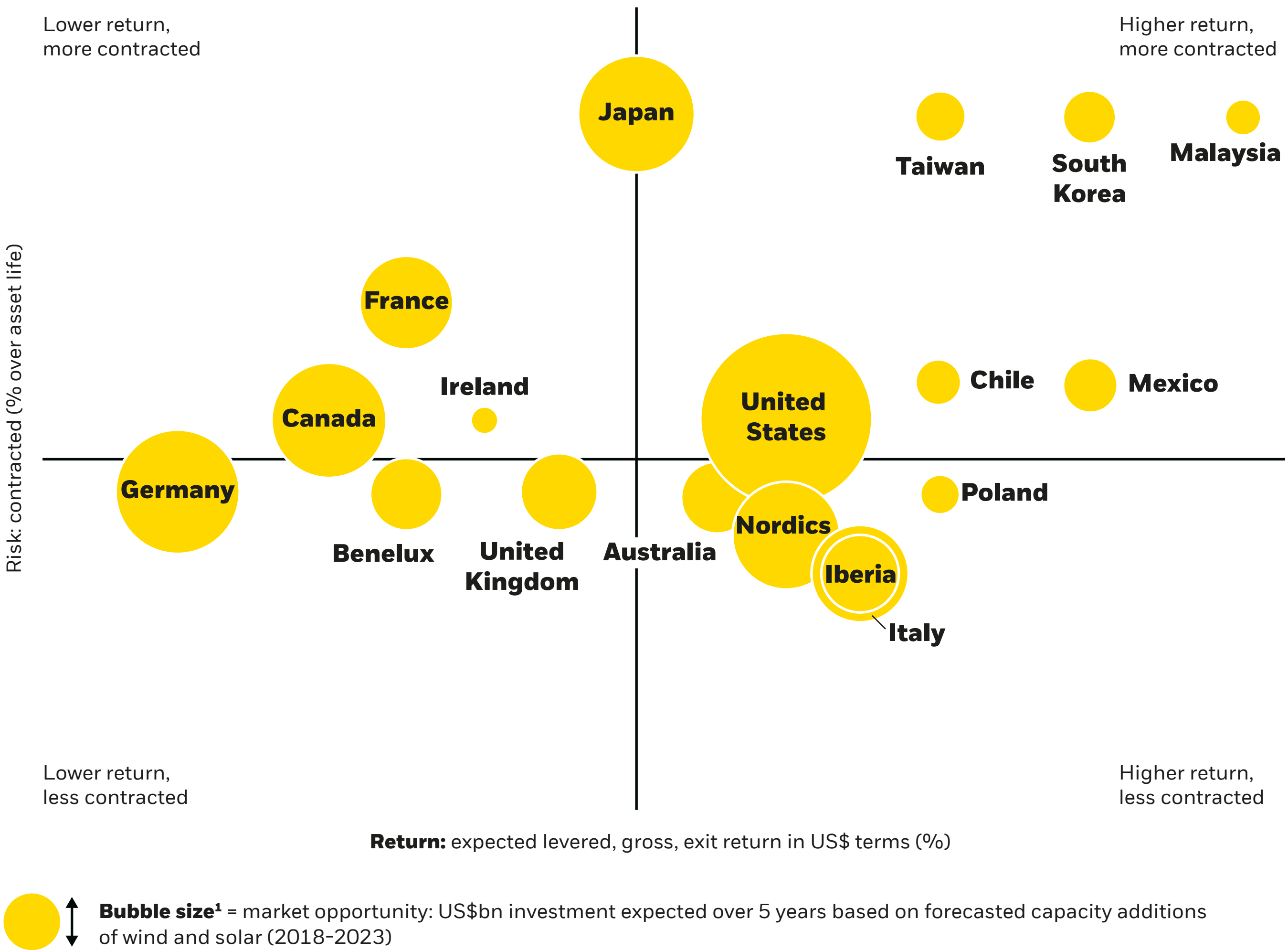
Office composite yield vs bond rates (German offices*)



* Berlin, Frankfurt, Munich, Hamburg equally weighted.
Source: PMA Forecast Service, Autumn 2019, BlackRock November 2019. Any opinions, forecasts represent an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This information should not be relied upon by the reader as research, investment advice or a recommendation. Forecasts may not come to pass.

Chart 7: Global renewables pricing environment

Power price risk and return, in the context of the addressable investment opportunity



Source: BlackRock, proprietary analysis performed by the Global Renewable Power Team, as of October 2019. Capacity market data is taken from Bloomberg New Energy Finance. This material is not intended to be relied upon as a forecast, research or investment advice, and is not a recommendation, offer or solicitation to buy or sell any financial instrument or product or to adopt any investment strategy.

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3 Changing with the future

Real Assets serve as the building blocks of a changing world. Impacted by change as technological advances accelerate, urbanization continues, environmental, social and governance (ESG) concerns intensify and global population grows and ages, albeit the rate of growth is slowing (projected to reach almost 10 billion by 2050 from 8 billion today[5]). These transformative trends are driving society's increasing demand for Real Assets but also changing the nature of this demand, in turn influencing the relative attractiveness of sectors within the asset class. Furthermore, these drivers are supporting the increasing investment demand for the asset class as demographic trends are increasing pension savings, and retirement rates drive demand for income producing assets.

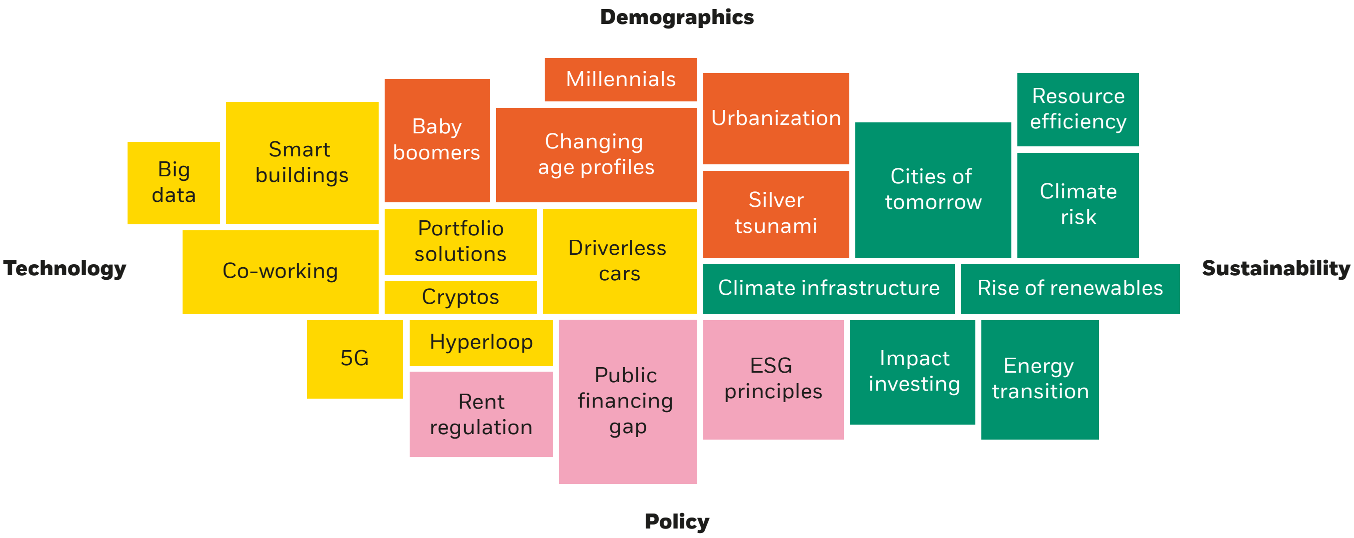
Within infrastructure, we see investable themes around the global energy and power transition, the public financing gap, the rise of digital infrastructure and the investment implications of smarter and more densified cites. Currently, the global power and energy transition is driving deal flow. The public financing gap remains but associated attempts to invigorate public private partnership models remains challenged. At the same time opportunities are opening in digital infrastructure in the context of smart cities.

Within real estate, emerging sectors are increasingly in favour, as exemplified in the living and healthcare spectrum backed by resilient demographic and urbanization trends. Capital invested into these sectors is at record levels. These sectors tend to be more operationally intensive, changing the risk profile for investors. Traditional sectors, meanwhile, are evolving amid developments such as the rise of flexible office providers and continued e-commerce pressures.

Sustainable investing considerations, including climate risk, energy performance and community impact, are increasingly in focus in Real Assets and are driving a greater integration of such factors into investment and asset management strategies.[6] ESG integration efforts and reporting reached a new high in 2019 and we expect this momentum to continue. Sustainability considerations could also put limits on the expansion of e-commerce, since the delivery of food and other goods to home conflicts with the increasingly ESG-conscious millennial market which remains a major target market for these services.

As we enter a new decade, investors will likely see rapid global changes ripple across Real Assets, as technology and sustainability increase their impact on the markets. The dimensions of secular change we have identified in Chart 8 — demographics, sustainable investing themes, technology and policy — are causing a level of disruption we have never seen before.

Chart 8: Changing with the future
The dimensions of secular change



Source: BlackRock Real Assets Research.

5 Derived from total population. Population source: (1) United Nations Population Division. World Population Prospects: 2019 Revision, (2) Census reports and other statistical publications from national statistical offices, (3) Eurostat: Demographic Statistics, (4) United Nations Statistical Division. Population and Vital Statistics Report (various years), (5) US Census Bureau: International Database, and (6) Secretariat of the Pacific Community: Statistics and Demography Programme. **6** BlackRock Investment Institute: The core role of private markets in modern portfolios. March 2019.

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Global Target Market Analysis – Boston, Berlin and Sydney offices to outperform

With real estate markets becoming increasingly international, investors can now consider how best to access relative value opportunities on a global basis in order to improve portfolio resilience and enhance returns. Although long-term investors maintain a substantial home bias in real estate investment, geographical diversification is rising steadily. The hunt for international real estate is partly driven by the greater volume of capital chasing this asset class as global pension assets grow and institutional allocations increase. With the investable universe expanding more slowly than demand, risk/return dynamics are encouraging investors to allocate capital globally. Global diversification could potentially help reduce volatility and improve portfolio resilience, as highlighted in Chart 9. An international approach can also potentially enhance both beta returns and opportunities for alpha generation.

In 2019, we released the *BlackRock Global Target Market Analysis*,[7] a proprietary market ranking framework for monitoring and projecting performance and risk across more than 50 markets for the four main global property types: office, retail, industrial and multifamily.

The key parameters for the framework are as follows:

Focus on cities

Experience teaches us that, notwithstanding some obvious common ground (e.g. currency), there are very different dynamics underpinning the development, pricing and future expansion of different cities within the same country.

Return ranking, risk ranking

More than 20 variables are weighted according to the team's view on their significance as an influencer of mid-term (five-year) risks and returns.

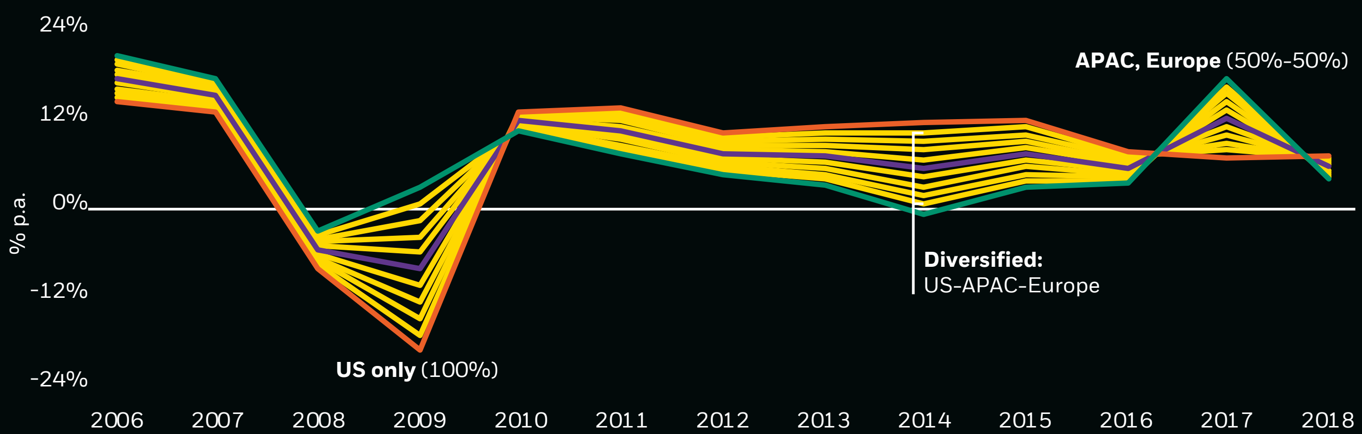
Key variables

We use fundamental and capital market factors to make adjustments to forecasts for net operating income (NOI) growth and dividend payouts, constructing return profiles.

Sector granularity

Structural changes are impacting certain property types in a similar way, regardless of the regional market considerations. To separate out the decisions on sectors from those on markets, our target market analysis covers each sector individually.

Chart 9: Hypothetical global portfolio returns
Portfolio Returns (USD)



Source: MSCI IPD, BlackRock (July 2019). Regional portfolio represents the investment universe as reported by MSCI IPD. Calculations are based on the full data set where there is a common historical span (2006 - 18). The figures relate to past performance. Past performance is not a reliable indicator of current or future results.

7 BlackRock Global Real Estate: A world of relative value, Target markets 2019.

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Regional market outlooks

North America

Economic conditions

The US economy slowed over the past year, but is still growing near its 2% potential. Elevated geopolitical risks are holding back economic activity. A comprehensive US-China trade deal does not look imminent, despite a "stage one" accord being reached. Impeachment proceedings and a presidential election add further uncertainty, as does recent military escalations in the Middle East. On the other hand, monetary stimulus has supported growth and should continue to do so. We expect a monetary policy pause in 2020, but if the Federal Reserve moves at all it will likely be to cut rates. While slowing global growth during 2019 provided a headwind for the US economy in 2019, we are witnessing a mild pickup of global growth. All in all, we expect another slow but steady year out of the US economy.

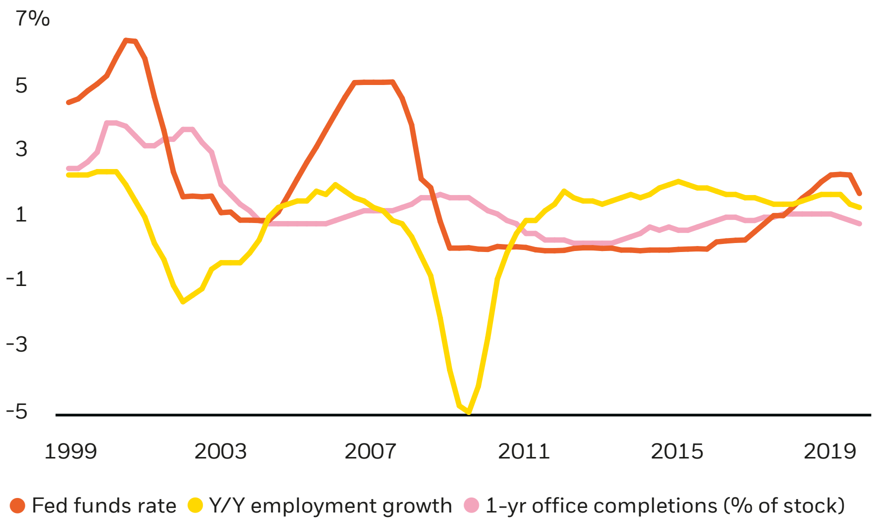
Real estate: everyone loves logistics, policy problems for apartments and a reset for retail

We expect income growth and yield to drive healthy single-digit returns for unlevered real estate at the asset level. Cap rates will likely remain stable as low global interest rates counter any upward pressure from slowing growth. In fact, recent bidding activity has an element of market capitulation as some investors are accepting even lower going-in cap rates in this lower rate environment. Tenant demand is strong enough to support modest rent growth across all four property types, but not strong enough to trigger a lot of new supply.

In 2019 every industrial (i.e. logistics) portfolio coming to market traded at or above expectations. Despite compressed cap rates, we still believe industrial will outperform because we see continued upside to rents. Apartments and office should market perform, but the market story is quite different. While we expect some secondary and tertiary apartment markets to perform well, we prefer primary, urban office markets. Retail is our strong conviction underweight. Retail is held back in part by landlords' limited leverage with tenants and a reluctance to make the capex needed to support modern tenant demand. More stores are opening than closing in the US, but those opening are much smaller than the ones that are closing. Many legacy big-box retailers are still grappling with online competition and highly indebted balance sheets, heightening challenges in the mall segment in particular.

Investors can potentially generate above-average income growth by favoring markets with strong in-place demographic and economic drivers — that is, cities with an affordable live-work-play value proposition for employers and residents alike. Markets such as Denver, Seattle, Austin and Nashville are positioned for sustained performance. These markets are beneficiaries of corporate expansions seeking the right mixture of talent access, quality of life and business climate. Bear in mind, however, that several markets that score well on these points have been victims of their own success. Amid high rents and pressure for action by policymakers, New York, California and Oregon have all enacted some form of state-wide rent control. This is challenging income growth and, in some cases, resulting in lower valuations of properties. However, we see a wide dispersion of rent control measures being enacted and the nuance is informing varied degrees of concern across markets.

Chart 10: Supportive fundamental backdrop for US CRE



Source: US Bureau of Labor Statistics, Federal Reserve Data, REIS, as of September 2019.

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Infrastructure: power and energy transition continues apace

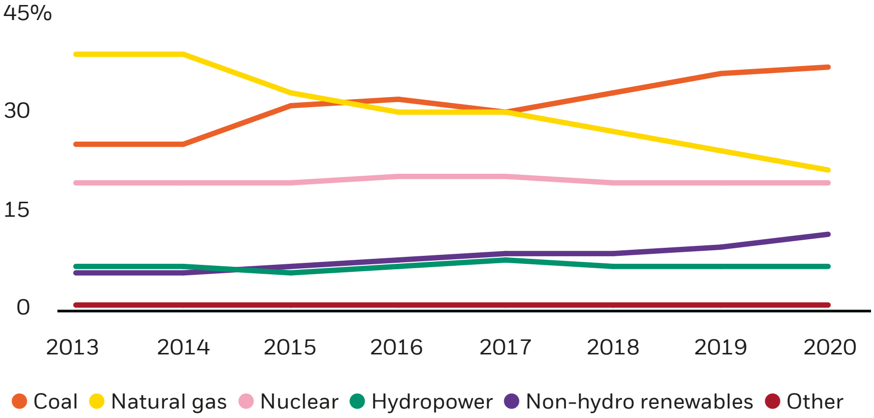
The multi-year makeover of the power and energy sectors — a global trend with some US-specific elements — is ongoing. Abundance of both renewable and traditional energy and technology advances are driving an energy renaissance in the US. Higher production is meeting the growth of demand for liquefied natural gas (LNG), particularly as many state utilities are retiring coal power plants for natural gas. International demand for natural gas is also supporting stronger LNG export volumes, a trend that we expect will provide investment opportunities in the transportation and processing space.

Meanwhile, the renewable space is maturing. While wind has led the way in new development in recent years, solar technology is now improved to a point where development should be much more rapid over the next few years. Federal policy is a moderate headwind, as federal tax credits are phasing out at the end of the year. These tax credits had benefited wind projects in recent years, and there is evidence that many developers have rushed to develop projects before the benefit expires.

Advances in battery technology are starting to move the needle on larger solar projects, as exemplified by Florida Power & Light Company pursuing the largest battery energy storage project in the world. Additionally, transmission will be a major investment class going forward. States and corporates are a tailwind. Almost 75% of US states have a renewable policy standard in place.[8] This has compelled significant advances in renewable instalments and coal phase-outs among utility companies nationwide. Many US companies have become more engaged in corporate power purchase agreements as well.

Chart 11: Short-Term Energy Outlook, November 2019

US electricity generation by fuel, all sectors (%)



Source: US Energy Information Administration, Short-Term Energy Outlook, November 2019.

Europe

Economic conditions

The European economy slowed in 2019 driven by weakness in the industrial sector resulting from the global manufacturing slowdown and persistent external geopolitical uncertainty. The slowdown has been more pronounced in Germany due to falling industrial production while in the UK, Brexit uncertainty has slowed business investment. France showed ongoing resilience, and Italy and Spain both remained stable. Economic growth is still supported by a resilient services sector, strong labour markets, accelerating wage growth and robust domestic demand.[9]

We see moderate growth and a lower rate environment for longer in Europe as supportive for Real Assets.

Real estate: fundamentals remain healthy

An extended European real estate cycle is benefiting from recent monetary policy support. Occupier demand remains healthy despite the recent economic slowdown. In the office sector most new supply in key markets is being absorbed, much of it through pre-let activity.

Demand from occupiers is expected to stay strong into 2020 and with vacancy rates at record lows in most markets positive rental growth is expected for the medium term.

When we finally see a resolution to Brexit the UK could offer attractive relative value in comparison with other European markets. Office yields in Central London are significantly higher than in other core European markets with an historically high spread to government bonds of almost 400bps.[10]

The logistics sector is expected to continue to be well supported by the reconfiguring of retailer supply chains and should outperform other sectors over the medium term, driven by stronger yield compression. The residential and alternative sectors also continue to attract investment and consolidate as investors align their strategies with long-term structural trends. Retail is hit by weaker rental expectations and the weakest investor sentiment on record and will continue to be the underperformer during 2020.

Investment activity in European commercial real estate was strong in 2019, largely in line with 2018, except for the UK where activity for the year-to-Q3 2019 was the slowest nine-month period for investment since 2013. The investment environment continues to be competitive and in terms of pricing, yields are at historical lows.

8 Source: National Conference of State Legislatures; BlackRock, as of December 2019. **9** Source: Figures from Oxford Economics Forecasting, November 2019. **10** RCA European Capital Trends – Q3 2019.

Yield compression which has been a key feature of this cycle was expected to come to an end but with interest rates staying lower for longer and more capital looking to enter the European market compression could continue for the best assets in the year ahead, pushing capital values even higher (see Chart 12).

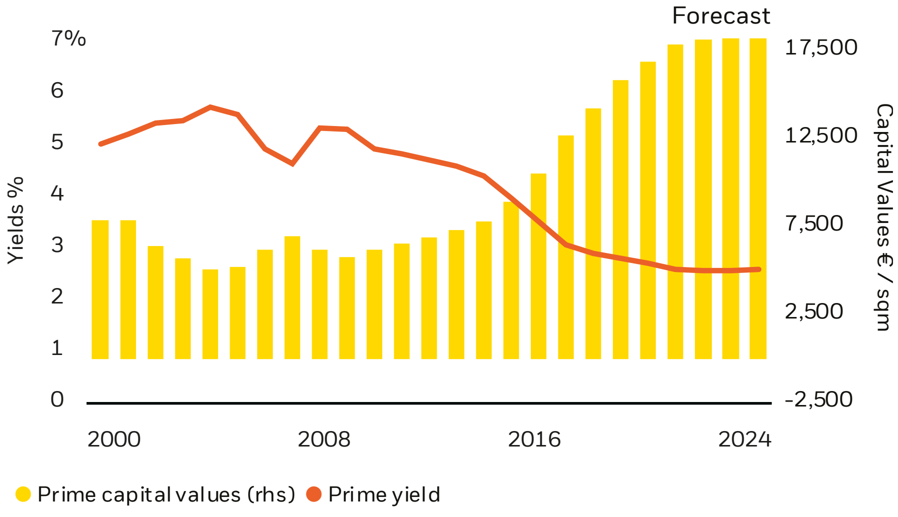
At this point in the cycle, remaining disciplined is critical. We prefer sectors offering cyclical and structural opportunities, like student accommodation and logistics. We favour secured income and cash-flow generative assets and focus on liquid and supply-constrained markets, especially when it comes to repositioning strategies.

Infrastructure: growing demand for clean energy

European renewables continue their steep growth trajectory.[11] The third quarter of 2019 marked a significant milestone with renewable energy sources generating more electricity in the UK than conventional fossil fuel fired power plants. The cost of offshore wind projects is also falling rapidly across Europe due to the fast pace of technological innovation, allowing the renewables industry to reduce costs year over year. Politics have also been instrumental in the rapid rise in renewable energy production and will continue to do so.

The growing trends of urbanisation and increasing environmental awareness are driving demand for more environmentally friendly transport with regulation becoming more supportive to the sector. The European Union's target to reduce greenhouse gas emission from transport by 60% by 2050 will necessitate an inevitable change to the way we move around our cities. The telecommunications sector remains buoyant with a significant broadening of the investment opportunity set. This reflects the growing demand for the digital infrastructure necessary to support the insatiable demand for connectivity.

Chart 12: Lower yields can push capital values even higher
Capital values and yields (German offices*)



Source: PMA Forecast Service, Autumn 2019, BlackRock November 2019.
*Berlin, Frankfurt, Munich, Hamburg.
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The European public-private partnership (PPP) market has continued to show signs of weakness. Historically low interest rates have made it harder for public entities to demonstrate the value for money of new PPP projects. For simpler projects, particularly in social infrastructure (e.g. schools), local authorities are reverting to design-build schemes that are less expensive than the traditional models. More technically challenging and/or capex-intensive projects, particularly in broadband infrastructure, ports and toll roads, continue to be awarded as PPPs.

Asia Pacific

Economic conditions

Across the Asia Pacific (APAC) region, demand growth will likely see only a moderate uptick in 2020, tempered by the slowing global cycle, rising trade barriers and local instances of civil unrest. All this is driving a considerably more diverse pattern of local demand growth. Japan continues to run firm given a domestic structural recovery. Australia moves into a more confident domestic upswing. China, South Korea and Singapore moderate with the global trade and manufacturing cycle. Meanwhile, Hong Kong faces a challenging economic downturn, affected by trade disruptions and continuing civil unrest. Nevertheless, there remains a broad and compelling APAC growth story that will persist for some years, supported by firmer demographic trends; rising incomes and wealth; and deepening capital markets and investor appetite.

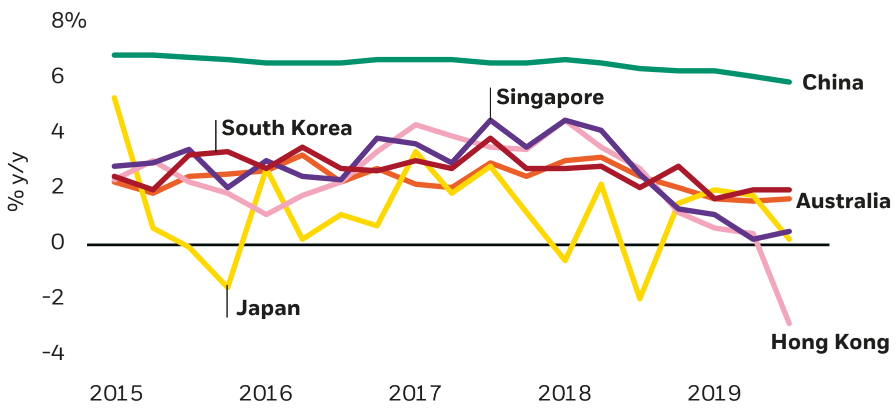
Real estate: understanding local idiosyncrasies is critical

Real estate markets in the APAC region are marked by a diverse set of very localized demand and supply trends, driving varied outcomes. For APAC investors, the focus for 2020 is still largely three-fold. Late-running market segments with comparatively higher yields still have some scope for cap rate compression ahead, particularly where these markets are seeing firmer cyclical demand (parts of Australia) or recovery from recent supply (Singapore, Korea).

11 BlackRock Infrastructure Solutions Infrastructure Market Update – Q3 2019.

Meanwhile, specific APAC markets are on track for sustained rental gains, given a favourable mix of robust demand and/or lagging supply (select office markets in Japan and China). That said, challenging conditions will drive some degree of pricing correction, particularly in Hong Kong, where investor focus will be shifting towards value and potentially distressed opportunities. More broadly, medium-term prospects in this region remain firm, given continued demand growth, uneven supply gains and improving market depth.

Chart 13: A diverse growth profile across regions
Real GDP: APAC major economies



Source: Bloomberg (December 2019). Data is latest available as of September 2019. **The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results.**

Infrastructure: rapidly emerging demand

Given robust APAC demand growth, the fundamental issue relates to the sizeable gap between demand and supply for new infrastructure. This gap persists across all key Asian markets and transport / utility sectors. Indeed, consumers are specifically seeking out greener renewable energy sources. Meanwhile, rising social awareness is elevating demand for more inclusive social infrastructure, from healthcare to public housing.

The APAC market landscape is emerging swiftly, as investors look for steady income streams backed by the expanding pool of Real Assets across the region. The initial focus remains on the transparent, well-regulated markets of Australia and Japan, but the improving regulatory framework is opening new opportunities in Taiwan and South East Asia.

In a growing APAC market, infrastructure opportunities extend to both equity and debt exposures. In newer markets with less-established regulatory regimes, the debt exposure provides sensible a risk profile for more conservative investors.

Latin America

Economic conditions

The region continues to build on foundations that support economic growth. Advancements in political and institutional stability, and proactive government policy to spur economic growth such as Columbia's 5G program and Brazil's refocused efforts on pension reform are resulting in a more constructive outlook. Most countries should benefit from improving economic performance next year. However, current global conditions, namely modest global growth pose challenges for the export-intensive region. In Mexico, cancelled infrastructure projects such as the New International Airport for Mexico City, fiscal austerity and a three-year suspension of energy contracts resulted in slower economic growth in 2019, showcase that risks still do remain for investors, but a strong consumer, a more favorable Mexico-US trade outlook and overall business confidence paint an attractive 2020.

Real estate: opportunities across region

Commercial real estate investment maintains upside potential. Brazil and Mexico remain the bulk of Latin American real estate deal flow. According to data from RCA as of Q3 2019, the two countries accounted for over 75% of the investable market year-on-year. The region experienced a sizeable slowdown in transactions over the past year owing to political and economic developments. However, the slowdown appears to be ebbing, and should likely stabilize to improve in 2020. For investors with a long-term horizon and higher risk tolerance, these markets provide an opportunity to invest in idiosyncratic themes.

Infrastructure: PPPs have attractive long term potential

Infrastructure development policy across Latin America is providing compelling opportunities for investors. With more infrastructure need than available public capital, regional governments are increasingly turning to investors to partner with and invest in economic growth improving projects from roads to hospitals. Even in Mexico, where the administration this year backed away from expensive infrastructure projects, investors are benefiting from more openness to public private partnerships. This is evident across the region, with Columbia's 5G program and Brazil's recent public oil auctions, which will require supporting infrastructure to support.

Even amid political changes and the external turbulence buffeting emerging markets, the economic outlook is constructive. Manageable levels of inflation is allowing more central bank accommodation. Combining this with attractive demographics and a deepening of government transparency, the region should continue to develop into a more active and compelling region for Real Assets investors.

Implications for investors

1

Cycling slowly:

With a different sort of cycle, strategies need to adapt.

In today's slowly cycling market, we advocate creativity with discipline. The ability to develop creative new strategies whilst maintaining discipline is critical. Discipline remains at a premium and the ability to systematically execute creative strategies is crucial. Focus should remain on income growth, value creation, and risk-adjusted returns.

2

Relatively attractive:

Seek to benefit from global dispersion.

We currently see a diverse world of opportunities. Markets are moving through different cyclical phases and at different paces, reflecting local trends in demand, supply, policy and political dynamics. Divergent markets present opportunities to exploit different market conditions in 2020 and beyond. It further highlights the importance of active market selection.

3

Changing with the future:

Dig deeper on issues of sustainability and technological change.

The world of ESG investments have moved well beyond investor preference, helping produce positive outcomes for investors, especially through higher investment returns. More than ever, an integrated Real Assets approach offers a unique platform for creating value in both real estate and infrastructure.

Furthermore, technological change has never been greater. Within both real estate and infrastructure, technology is disrupting Real Assets, structurally changing the investment environment and creating new challenges and opportunities for investors. Investors need to have a proper understanding of the role technology will play in portfolio resiliency.

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Real Assets

410+
professionals

27 offices
globally

US$52bn+
in client assets

Source: BlackRock, as of December 2019.

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